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ANNUAL REPORT

OF

MARSHALL FIELD & COMPANY

AND SUBSIDIARIES

YEAR ENDED
DECEMBER 31, 1937

CORPORATE OFFICE

The Merchandise Mart
222 North Bank Drive : Chicago, Illinois

BOARDS
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M3681

MRB
CORP. FILE

In Memoriam

JAMES O. McKINSEY

1889—1937

Chairman and Director

Marshall Field & Company

MARSHALL FIELD & COMPANY

BOARD OF DIRECTORS

FREDERICK D. CORLEY
MARSHALL FIELD
STANLEY FIELD
CHARLES H. SCHWEPPE
JAMES SIMPSON
JAMES SIMPSON, JR.
JOHN P. WILSON

OFFICERS

President
FREDERICK D. CORLEY

First Vice-President
HUGHSTON M. McBAIN

Vice-Presidents
CHARLES C. BUNKER
PERCY WILSON

Comptroller
KENNETH E. ARMSTRONG

Secretary-Treasurer
EARL KRIBBEN

Assistant Secretary
HOWARD M. PACKARD

Assistant Treasurers
JOHN C. GOODALL
WILBUR C. MUNNECKE

Transfer Agents
CONTINENTAL ILLINOIS NATIONAL BANK AND TRUST COMPANY OF CHICAGO
CHICAGO
GUARANTY TRUST COMPANY OF NEW YORK
NEW YORK

Registrars
THE FIRST NATIONAL BANK OF CHICAGO
CHICAGO
BANKERS TRUST COMPANY
NEW YORK

TO THE STOCKHOLDERS:

I submit herewith the annual report of your Company for the calendar year 1937. Included in the report are financial statements comprising the balance sheet, profit and loss statement, earned and paid-in surplus statements and statements of reserves, all on a consolidated basis, and a letter from your Company's independent auditors.

The results of the year's operations, by Divisions, as compared with 1936, are as follows:

	1937	1936
Retail Division	$5,029,090	$4,836,738
Manufacturing Division	5,679,209*	28,850
Real Estate Division	25,297*	446,917*
Profit or loss from operations before interest and special charges	$ 675,416*	$4,418,671
DEDUCT —		
Interest charges	$ 665,105	$1,135,029
Financial reorganization expense	—	104,897
Special compensation of James O. McKinsey	313,930	—
Federal and State income tax reserve	—	300,000
	$ 979,035	$1,539,926
Net profit or loss for year	$1,654,451*	$2,878,745

(*Indicates a loss)

The results of operations shown above are after deducting provisions for depreciation of buildings and equipment, etc., of $2,421,375 in 1937 and $2,377,468 in 1936.

Our sales for the past two years, including real estate income, have been as follows:

1936	$106,135,693
1937	$100,044,813
Decrease	$ 6,090,880

If the sales of discontinued lines of business are eliminated from both years, the sales of 1937 exceeded the sales of 1936 by 5.1%.

RETAIL DIVISION

The Retail Division consists of the Main Retail Store, State Street, Chicago; suburban stores located at Evanston, Oak Park and Lake Forest, Illinois; Frederick & Nelson, Seattle, Washington, and two small stores located at Chicago Heights, Illinois, and Watertown, South Dakota.

The Retail Division has been under the active management of the same executives who have been operating it successfully for a great many years.

All of our retail stores had a successful year, this Division showing a net profit of $5,029,090 for 1937 as compared with $4,836,738 in 1936 and $3,426,861 in 1935. In every year since the Company was founded, with the exception of 1932, this Division of the business has operated at a profit.

The gross margin of profit in all stores was slightly higher than in 1936. However, higher taxes, increased operating expenses and higher wage levels adversely affected net profit percentages. Many of the increased expenses were non-controllable in nature.

Retail Division sales showed a material increase over sales in 1936, which in turn were greater than the sales in 1935. The number of sales transactions during the year in all units of the Retail Division was substantially higher than in the prior year, and the average sales check was also larger.

During the year, ten new elevators were added to the Main Retail Store in Chicago; air conditioning equipment was installed in the Oak Park Store, and some new equipment was procured for the delivery fleet. A number of minor changes also were effected which should tend further to improve our service and make all our stores increasingly attractive and convenient to customers.

The small store which your Company formerly owned in Alliance, Ohio, was sold as of December 31, 1937.

MANUFACTURING DIVISION

The Manufacturing Division consists principally of fifteen mills in the United States and one each in the Philippine Islands, Puerto Rico and China, and also embraces various converting and importing activities. Its products include a wide variety of textiles, floor coverings and apparel.

The operating results of the Manufacturing Division after its reorganization were not successful, as shown by this statement. It may be stated that under any circumstances the general course of business and prices would have caused a serious loss in

this Division. To aggravate this condition, however, the services of an entirely new management had been established on a scale of overhead expense, including leases and salaries, that the volume of business entirely failed to justify.

During the early part of the year, production of all kinds of goods was at a high level, commodity prices were advancing, and a feeling of confidence pervaded the business world. Inventories were rapidly increased to meet the increasing demand for goods and to correct the situation existent during 1936, when we were not always able to deliver merchandise to our customers at the times and as rapidly as they demanded it.

Unfilled orders on January 1, 1937 were the largest in years, and the productive capacity of certain mills had been booked for considerable periods in advance. An operation of this type necessarily requires the maintenance of a sufficient stock of raw materials to cover all orders on hand and in sight. Our commitments extended considerably beyond this point. Beginning in the late spring of 1937, conditions changed with almost unprecedented swiftness. By the advent of early fall there had been a drastic decline in commodity prices, especially in the textile field, and orders shrank in an alarming degree, particularly for advance business. We were severely penalized by cancellations and by the failure of prospective fall orders to materialize in the amounts anticipated.

The declines occurring in three raw materials which we owned in large quantity may here be cited to illustrate the severity of the situation. Cotton, which had reached a level of 14½ cents a pound in March, was selling by the end of the year for 8¼ cents; silk declined in the same period from $2.01 a pound to $1.58 a pound, and the price of wool receded during this time from $1.05 a pound to 81 cents a pound.

The precipitous decline in the fourth quarter of the year in many lines of business, and particularly in the textile industry, was as great as any in business history. The excessive overhead costs and the decrease in production and sales, together with lower selling prices and necessary mark-downs on our year-end inventory, which as usual was taken at the lower of cost or market, were responsible for the very disappointing results of the year's operations.

Our inventory of raw and finished goods on hand in the Manufacturing Division at the year end stood at $10,410,000, or approximately 12% less than the year before. At December 31, 1937, our future commitments for raw materials and finished goods were lower than was the case a year earlier, and adequate provision was made for losses on goods on order. These future commitments are not now regarded as being excessive, and your directors believe that merchandise inventories and future commitments at December 31, 1937 are valued on a sound basis.

Since last December we have entirely reorganized the management of the Manufacturing Division and now contemplate that operations will be conducted on a greatly simplified basis. We have already effected large reductions in administrative, overhead and selling expenses, and hope that in the future this Division will produce results satisfactory to the stockholders. The further reorganization or discontinuance of certain activities in the Manufacturing Division which have not shown a consistently sustained profit over a period of years is under consideration. It has been thought prudent to establish an additional reserve of $2,500,000, which has been charged to earned surplus as of December 31, 1937, to cover any losses that might be sustained in the process of eliminating such activities if and when so decided. This supplemental reserve should be adequate to cover these contingencies, and it is hoped will prove to be in excess of future requirements.

While certain of our mill properties have been disposed of during the year, we have not sold and do not now contemplate the sale of any of the mills in our main integrated southern group located in North Carolina and Virginia.

REAL ESTATE DIVISION

The Real Estate Division consists principally of The Merchandise Mart and the "Annex" Office Building.

The Merchandise Mart continued to show progress throughout the year. Income was increased 15%, which was sufficient, despite the additional expense resulting from increased occupancy, to enable the building to show a greatly improved result.

A major problem in the management of the Mart has been the necessity of continuing the conversion of large unfinished floor areas released by the Manufacturing Division into finished corridor-serviced units for leasing to tenants. An additional area was vacated during the spring, when that Division consolidated its office, accounting and warehouse operations in New York. This resulted in bringing the total area released by your Company since 1935 to 974,000 square feet. The Mart is now over 78% leased, about 67% of its space being used by other tenants and only 11% by the Company, as against over 42% formerly so used.

An important 1937 improvement of this property was the completion of the installation of six new elevators early in the year. The Merchants and Manufacturers Club was organized, with attractive quarters in the building, and is already proving to be a valuable addition to the services provided for tenants and buyers. Many other lesser improvements were made throughout the building.

The daily working population within the Mart at mid-year was 24,618. This made possible the development of an arcade of retail shops on the second floor, all of which

have been rented. Both volume of sales in retail shops on the lower floors, and wholesale buyer attendance on the upper market floors showed encouraging increases. Total tenant leases in the building at the year end were 703 in number, an increase of 87 over the prior year. During the year 426,652 square feet were leased, which together with leases made during the previous year, exceeded all area vacated by Company units.

The "Annex" Office Building, which also houses our Store for Men, showed substantial improvement in operating results for 1937. This unit should continue to contribute profitably to the Real Estate Division.

FINANCIAL MATTERS

During the year our funded debt was reduced by $1,000,000 through the payment of the maturing instalments of our serial bank loan, and at the year end stood at $18,000,000, constituted as follows:

Serial Notes, maturing at the rate of $1,000,000 a year from 1938 to 1941, inclusive, average rate of interest slightly over 2½%	$ 4,000,000
First Mortgage Serial Bonds, maturing at the rate of $1,000,000 a year from 1942 to 1951, inclusive, interest 4%	10,000,000
First Mortgage Serial Bonds, maturing at the rate of $1,000,000 a year from 1952 to 1955, inclusive, interest 3% through 1941; 4% thereafter	4,000,000
Total	$18,000,000

Interest charges were reduced approximately $470,000 in 1937, due to the refunding of our debt in late 1936.

During the year preferred dividends of $2,411,931.25 were paid, covering all dividends due through December 31, 1937 on both the prior preferred and 6% cumulative preferred stock issues.

Taxes continued their upward trend during the past year, and sums paid to the Federal and to the various state and local governments amounted to approximately $4,000,000. Your Company's tax accruals during 1937 amounted to 4c of every dollar of net merchandise sales, or almost 9c per dollar of invested capital. They amounted to approximately $13.46 per share of preferred stock (both classes), or $2.42 per share of common stock.

At Mr. McKinsey's death on November 30, 1937, the contract with him dated October 7, 1935, as amended January 5, 1937, automatically terminated except for the

right of his estate, on or before December 31, 1938, to purchase 10,000 shares of unissued common stock at $10 per share. or to receive a sum of money equal to the amount by which the market price of such 10,000 shares exceeds $10 per share.

Mr. McKinsey exercised only a portion of the stock options contained in his contract. He purchased a total of 20,000 shares of unissued common stock at $10 a share and also elected to receive a sum of money equal to the amount by which the market price of 20,000 additional shares of common stock exceeded $10 per share. As noted in the third quarterly report for 1937, the sum of $313,929.90 was therefore credited to him on the books of the Company. Of this amount $13,929.90 was paid to him and the balance of $300,000.00 remains credited to his estate on our books. This balance will be held until the termination of two suits recently filed, which raise certain questions with regard to the contract.

PERSONNEL

The By-Laws of the Company were amended in December, 1937, and the office of Chairman was abolished. The Board of Directors designated Mr. James Simpson as Chairman of the Executive Committee. Mr. Frederick D. Corley, President of the Company, who has been in the employ of the Company since 1900, was made chief executive officer. Mr. Hughston M. McBain was elected First Vice-President and given charge of the Manufacturing Division. Mr. Charles C. Bunker, Vice-President in charge of the New York Buying Office, was recalled to Chicago to become General Merchandise Manager of the Main Retail Store. Mr. Percy Wilson, Treasurer and Real Estate Manager, was elected Vice-President in charge of Real Estate. Mr. Kenneth E. Armstrong, Secretary and Assistant Comptroller, was elected Comptroller, and Mr. Earl Kribben was elected Secretary and Treasurer.

Mr. John McKinlay resigned as a director of the Company on December 13, 1937.

The directors are grateful to our customers and to all members of the organization for their loyal support and cooperation during the past year, and look forward with confidence to a resumption of profitable operations in the future.

By order of the Board of Directors,

FREDERICK D. CORLEY, President

March 15, 1938.

MARSHALL FIELD & CO

CONSOLIDATED BALANCE

ASSETS

CURRENT ASSETS:			
Cash in banks and on hand		$ 2,225,867.90	
Receivables—			
Accounts receivable from customers	$12,196,052.53		
Rents, claims and miscellaneous receivables	659,896.41		
	$12,855,948.94		
Less—Reserve for doubtful accounts, etc.	561,423.00	12,294,525.94	
Merchandise inventories; quantities and condition determined by the company; priced at the lower of cost or market—			
Manufacturing Division merchandise, including raw materials and work in process of $4,228,751	$10,410,292.32		
Retail Division merchandise	9,965,547.87	20,375,840.19	
TOTAL CURRENT ASSETS			$34,896,234.03
PREPAID INSURANCE, SUPPLY INVENTORIES, ETC.			847,622.36
INVESTMENT SECURITIES, ETC.:			
Securities and cash deposited under construction agreements		$ 154,014.06	
Miscellaneous receivables, etc.		161,999.54	316,013.60

FIXED ASSETS:

Classification	Cost	Reserves for Depreciation and Amortization	Net	
Retail and manufacturing properties, etc.—				
Land	$ 899,809.52	$ —	$ 899,809.52	
Leaseholds	1,375,405.83	242,372.74	1,133,033.09	
Buildings and building equipment—				
On owned land	8,418,495.59	5,444,687.38	2,973,808.21	
On leased land	14,757,701.76	4,329,175.91	10,428,525.85	
Equipment	14,469,731.73	8,262,843.26	6,206,888.47	
Merchandise Mart (pledged under first mortgage)—				
Air rights and land	2,907,461.85	—	2,907,461.85	
Building and equipment	27,625,141.56	4,700,616.18	22,924,525.38	
TOTAL FIXED ASSETS	$70,453,747.84	$22,979,695.47	$47,474,052.37	47,474,052.37
GOODWILL, TRADE-MARKS, ETC.				1.00
				$83,533,923.36

ANY AND SUBSIDIARIES
HEET, DECEMBER 31, 1937

LIABILITIES

Current Liabilities:			
Accounts payable—			
Trade creditors	$ 2,351,595.41		
Customers' credit balances and sundry accounts payable	542,080.34	$ 2,893,675.75	
Liability to Estate of James O. McKinsey under option exercised in 1937		300,000.00	
Accruals—			
Salaries and wages	$ 923,419.47		
Local and miscellaneous taxes	2,643,926.29		
Other accrued expenses	632,433.10	4,199,778.86	
Reserve for Federal income taxes (subject to final determination by the Treasury Department)		571,480.63	
Current maturities of serial notes		1,000,000.00	
Total Current Liabilities			$ 8,964,935.24
Funded Debt:			
Serial notes, maturing $500,000 semi-annually from June 19, 1938 to December 19, 1941, inclusive, interest at rates from 2 to 3% (current maturities shown above)		$ 3,000,000.00	
First-mortgage serial bonds—			
Series One—4%, maturing $500,000 semi-annually from May 1, 1942 to November 1, 1951, inclusive	$10,000,000.00		
Series Two—3% to November 1, 1941 and 4% thereafter, maturing $500,000 semi-annually from May 1, 1952 to November 1, 1955, inclusive	4,000,000.00	14,000,000.00	17,000,000.00
Reserves:			
For loss on commitments		$ 212,437.75	
For possible loss on contemplated disposition of properties, future inventory losses, etc., in connection with reorganization of Manufacturing Division		3,569,682.89	
For loss on subleases		432,230.23	4,214,350.87
Contingent Liabilities, Etc.:			
Under letters of credit—$350,000.			
Under long-term leases—rentals payable are at present approximately $1,200,000 per year.			
Under option—see pages 6 and 7 of President's letter.			
Capital Stock and Surplus:			
Prior preferred stock—			
Authorized 15,000 shares of $100 par value; entitled to 7% cumulative dividends; redeemable at $120 per share and accrued dividends.			
Issued and outstanding 8,965 shares		$ 896,500.00	
6% cumulative preferred stock—			
Authorized 296,190 shares of $100 par value; redeemable, if no prior preferred stock is outstanding, at $110 per share and accrued dividends; convertible until January 1, 1947 at the option of the holder at the rate of three shares of common stock for each share of preferred stock.			
Issued and outstanding 287,225 shares		28,722,500.00	
Common stock—			
Authorized 4,000,000 shares of no par value, of which 888,570 shares are reserved for conversion of 6% cumulative preferred stock and 180,000 shares are reserved for sale to officers and employees.			
Issued 1,659,335 shares, at stated value		15,396,675.00	
Paid-in surplus		5,001,898.65	
Earned surplus, of which $226,773.97 is restricted by reason of purchase of treasury stock		3,563,837.57	
Capital stock and surplus before deducting treasury stock		$53,581,411.22	
Less—Treasury common stock, 15,278 shares, at cost		226,773.97	
Capital stock and surplus, net			53,354,637.25
			$83,533,923.36

MARSHALL FIELD & COMPANY AND SUBSIDIARIES

Consolidated Statements of Profit-and-Loss and Surplus Accounts
For the Year Ended December 31, 1937

Consolidated Statement of Profit and Loss

NET SALES TO CUSTOMERS		$97,641,739.65
COST OF SALES AND OPERATING EXPENSES		98,291,859.30
Net loss from merchandising operations		$ 650,119.65
LOSS FROM REAL ESTATE OPERATIONS:		
Rental income from tenants	$ 2,403,073.97	
Operating expenses, less rentals charged to merchandising divisions	2,428,371.00	25,297.03
Net loss from operations before interest and special charges		$ 675,416.68
INTEREST AND SPECIAL CHARGES:		
Interest on funded debt	$ 633,250.00	
Interest on bank loans, etc.	31,855.19	
Provision for amount due to Estate of James O. McKinsey under option exercised in 1937	313,929.90	979,035.09
Net loss for the year		$ 1,654,451.77

NOTES:

(1) The net loss on merchandising operations represents a loss of $5,679,209 in the Manufacturing Division and a profit of $5,029,090 in the Retail Division.

(2) The provision for depreciation of buildings and equipment, etc., included as a deduction in the foregoing statement amounts to $2,421,374.84.

Consolidated Statement of Earned Surplus

BALANCE AT DECEMBER 31, 1936		$10,133,886.59
DEDUCT:		
Loss for the year 1937	$ 1,654,451.77	
Cash dividends paid—		
Prior preferred stock ($28.75 per share)	257,743.75	
6% cumulative preferred stock ($7.50 per share)	2,154,187.50	
Stated value ($5 per share) of 706 shares of common stock issued pursuant to plan of reorganization effective December 26, 1936, plus payment for fractional shares	3,666.00	
Provision for possible loss on disposition of properties, future inventory losses, etc., in connection with reorganization of the Manufacturing Division	2,500,000.00	6,570,049.02
BALANCE AT DECEMBER 31, 1937		$ 3,563,837.57

Paid-In Surplus

No changes were recorded during the year in this account.

MARSHALL FIELD & COMPANY AND SUBSIDIARIES

Consolidated Statements of Reserve Accounts
For the Year Ended December 31, 1937

Reserve for Possible Loss on Contemplated Disposition of Properties, Future Inventory Losses, etc., in Connection with Reorganization of Manufacturing Division

BALANCE AT DECEMBER 31, 1936, provided for loss on disposition of properties then contemplated	$ 1,270,758.99
DEDUCT—Loss on disposition of manufacturing properties, etc., during 1937	201,076.10
	$ 1,069,682.89
ADD—Provision for possible loss on disposition of properties, future inventory losses, etc., in connection with reorganization of the Manufacturing Division, charged to earned surplus	2,500,000.00
BALANCE AT DECEMBER 31, 1937	$ 3,569,682.89

Reserve for Loss on Subleases

BALANCE AT DECEMBER 31, 1936	$ 575,832.37
DEDUCT—Excess of rentals, taxes, insurance, etc., paid on subleased properties during 1937 over rentals received	143,602.14
BALANCE AT DECEMBER 31, 1937	$ 432,230.23

ARTHUR ANDERSEN & CO.

135 SOUTH LA SALLE STREET
CHICAGO

To the Board of Directors,
Marshall Field & Company:

We have made an examination of the consolidated balance sheet of MARSHALL FIELD & COMPANY (an Illinois corporation) AND SUBSIDIARY COMPANIES as at December 31, 1937, and of the statements of consolidated profit and loss, surplus and reserves for the year ended that date. In connection therewith, we examined or tested accounting records of the companies and other supporting evidence, and obtained information and explanations from officers and employees of the companies; we also made a general review of the accounting methods and of the operating and income accounts for the year, but we did not make a detailed audit of the transactions.

In our opinion, based upon such examination, the accompanying consolidated balance sheet and related statements of profit and loss, surplus and reserves fairly present, in accordance with accepted principles of accounting consistently maintained by the companies during the year under review, the financial position of the companies at December 31, 1937, and the results of their operations for the year ended that date.

ARTHUR ANDERSEN & CO.

Chicago, Illinois,
March 14, 1938.